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Economic Conditions
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General Business Conditions

THE business news of the past month is of the kind more generally associated with a boom than a depression, and in fact supplies good reasons for the opinion that the word "depression" no longer applies to the general business situation, however regrettably it must be used in connection with the unemployment and conditions in a few of the industries. Not since the years prior to 1929 has there been such a flood of wage and dividend increases and special year-end distributions, both for workers and shareholders. Publicly announced dividend declarations during November, mostly payable in December, have exceeded those of any other month on record, according to preliminary figures which indicate a total in the neighborhood of $800,000,000.

This does not signify, of course, that dividend payments for the whole year will set a record, for they may not be more than two-thirds of the 1929 total. The declarations are concentrated at this time, and increases in payments stimulated, by the graduated penalty tax laid upon undistributed corporate earnings in the last Revenue Act; this naturally induces the distribution of a substantially greater part of the year's earnings than would have occurred under previous tax schedules.

Overlooking the doubt as to wisdom of forcing these extraordinary disbursements, and the possibly restraining effect on corporate expenditures for capital goods, the stimulus to trade is unquestionable. Moreover, workers also are benefitting, and payments to labor are taking a jump which in the long run will represent a greater cash disbursement than the distributions to stockholders. Wage increases, affecting the entire steel industry, most of the woolen mills, cotton mills, automobile plants and others, have become front-page news, and have spread widely through the industries. The basic reasons for the increases are the short supply of skilled labor in many lines, the rising trend of earnings and living costs, and the desire of manufacturers to hold or increase their labor forces and to anticipate demands which might result in costly labor troubles.

Employment likewise is on the upgrade. Production has risen in many of the major industries, and in others operations have been maintained without check past the time when a seasonal decline usually occurs. Making allowance for seasonal conditions, the composite general business indexes for November are expected to set a new high for the recovery by a good margin, rising to the highest since the Fall of 1929. Most of these indexes will be close to the calculated "normal," which is assumed to represent prosperity.

Thus the industries are giving more work at higher wages. The farmers are doing well, with a liberal movement of livestock and cotton to market, and increased sales of dairy and poultry products, all at good prices. They are also receiving soil conservation payments. Finally, the rise in commodity markets, especially in industrial raw materials, is an outstanding and important development. It has stimulated forward buying not only in raw materials but in manufactured goods also, since finished goods now have to be marked up in price to cover the increased cost of materials and higher wages; and of course it gives an increased income to the producers of these staples, both in this country and abroad.

Best Holiday Season Since 1929

With this increased purchasing power flowing into consumers' hands, the holiday season will be the most cheerful since the onset of the depression. Trade evidently will be the best since 1929, in dollars, while the unit volume of goods sold in many lines will be greater than in 1929. The luxury lines are doing well. In New York stores, furs lead all departments in percentage of gain, and retail demand generally is for a better quality of merchandise than in several years. It is commonly expected that Christmas trade on the whole will exceed 1935 by at least 15 per cent, a figure well within the gains of recent weeks. In October depart-

ment store sales were 16 per cent over last year, and mail order houses and variety chains made even greater increases. Preliminary reports indicate November will show similar gains.

Business expanded rapidly in the last quarter of 1935, rising to the highest level then reached in the upswing, and the present increase of better than 15 per cent over last year, in both production and trade, represents a very substantial improvement. The rise a year ago was largely centered around the automobile industry, which made a great success of the Fall introduction of new models. This year the automobile is again giving strong support to business. As usual, improved cars are offered, in many cases at reduced prices although wages have been raised. Retail sales are ahead of last year, dealers want cars as fast as they can be built, and assembly operations have been steadily expanded to a level approaching the Spring peak, where they will be maintained for some time. Of course many industries are stimulated by the requirements of the automobile manufacturers for parts and materials.

However, the current improvement is less dependent upon automobiles than a year ago, for it is more widespread. The steel makers are drawing their orders from a greater variety of industries and have maintained ingot production for over two months at approximately 75 per cent of capacity, a six-year peak, compared with 55 in November last year. Railroad buying is more active, and in the coming year the railroads seem certain to take much more steel. Tin plate operations hold at a high level and miscellaneous demands are good, reflecting the improvement in farm implements and road machinery, hardware and steel furniture, electrical goods and other lines. Following general wage increases throughout the industry, price advances of $2 to $4 a ton for first quarter delivery have been announced, and these should stimulate forward buying, replace the orders which have been running off, and prevent any disturbing drop in steel operations for some time.

Announcements of plans to modernize and expand their plants continue to come from the steel companies. The Bethlehem Steel Corporation will spend $35,000,000 before the end of 1937, largely on a continuous rolling mill at Sparrows Point. Republic Steel Corporation will spend $15,000,000 on continuous mills at Cleveland, and Youngstown Sheet and Tube $10,000,000, all in addition to plans previously announced. Inland Steel will build the first blast furnace constructed in eight years.

Other industries, including the railroads, are spending more on equipment and machinery. The New York Central has ordered 100 locomotives, which with other equipment will represent an expenditure of $14,000,000. This is the largest order for locomotives since 1929. The St. Paul also has ordered 30 locomotives. Last year all the roads together bought only 83 locomotives, of all kinds. This is business progress of the most important kind. It adds to employment in the capital goods industries, and the new equipment will reduce the operating costs of the railroads.

The electrical equipment manufacturers are busy. Machine tool orders in October increased, and except for last July were the largest in any month since 1929.

Building contracts awarded during the first half of November made a better showing than in October, when a slackening of public works contracts brought the totals down. November usually shows a pronounced seasonal decline, but the daily average for the first half of the month was even with October, and privately financed contracts were close to the high for the recovery, and almost double a year ago.

The Boom in Textiles

The most sensational performance among the industries has been turned in by the textiles. Demand for cotton goods, even after many months of activity, seems insatiable. Although cotton mills are working at an all-time record rate spot goods and early deliveries are scarce, and buyers willingly pay premiums for them. In some cases buyers have booked through the second quarter of 1937. As a whole, mills are probably sold farther ahead than ever before and at profitable margins over cotton prices, even allowing for the wage increases. The situation is leading to the reopening of mills in New England which have not operated in some time, including four units of the failed Amoskeag Mills, which have been leased to the Pacific Mills and will be put back into operation.

The rayon mills are equally active. Demand for viscose yarn has absorbed all reserve stocks and keeps factories operating at capacity, while fabric sales and prices have both improved against the usual seasonal trend. Despite the tight market, yarn manufacturers have not raised prices except for the elimination of certain discounts effective January 1, and all the important companies have plant expansion programs under way.

The woolen situation has turned strong after a period of unsatisfactory margins, and Spring goods prices have been raised 15 to 27 cents a yard over the opening. Wage increases, advances in raw wool and taxes under the Social Security Act have raised costs; buyers therefore have accepted the higher prices as inevitable and bought freely, giving the mills a good backlog of orders. This willingness to operate ahead extends to clothing buyers as well, since clothing prices are moving up in turn. Raw silk also has risen and the business of the hosiery manufacturers, now the chief consumers of silk, is good; buyers of hosiery have been

anxious to cover forward needs also, but manufacturers have not been disposed to accept 1937 business at the old prices.

In all merchandise lines willingness to buy ahead is more general than at any time except in the boom of 1933. Prices of rugs and floor coverings have been raised. Furniture business is active with a price advance scheduled. Advance shoe sales are good. On some items of gift merchandise premiums are the rule for prompt deliveries.

Is the Upward Movement Too Rapid?

A situation in which there is competitive bidding for spot merchandise, active buying for future needs, widespread expectation of higher prices and perhaps scarcity of goods, and a short supply of skilled labor prompting manufacturers to raise wages, is of course a novelty in recent business experience in this country. In some respects it recalls the Spring of 1933, when prices in many lines were advancing rapidly, forward buying was the rule, and operations in some industries were driven to capacity even in the midst of depression. The boom at that time proved short-lived because over-buying speeded up the advance too rapidly, and consumers could not pay the higher prices demanded.

It would assume a great deal to expect a vigorous upward movement such as is now being experienced to continue without reaction. After any unusual spurt of buying and rising prices, as now in the textiles, the crest naturally will be passed, and there are always people holding for a rise who sell when they believe the rise is over. Moreover, after a long period of abnormally active buying there is inevitably a dull period, and the incentive to forward buying disappears. The appearance of scarcity is apt to prove illusory, since relief may be had both through increased production, and because the buying turns out to be running ahead of consumption. This view of the situation inspires caution, as suggesting a temporary slowing down in the forward movement.

Sound Elements in the Situation

However, the analogy with 1933 does not carry far. The present position is plainly much stronger. The boom in 1933 was stimulated by arbitrary increases in costs and prices caused by legislation,while the present rise is attributable to natural influences of supply and demand. Business improvement is on a vastly broader base, and consumers therefore are better able to sustain the increase in living costs. Farm prices are practically at a parity with industrial prices, according to the formula that was embodied in the Agricultural Adjustment Act, and farm purchasing power has increased correspondingly. The industrial improvement has extended to virtually all the industries, including those making capital goods; employment has gained, and with costs and prices in better balance the production and exchange of goods up to the limits of the capacity to produce is vastly more practicable. Debts are lower and all property values higher, and the national income (1936 over 1933) has increased by some fifteen billion dollars.

Moreover, in other respects the situation is not such as to produce or render likely a serious or prolonged reaction at this stage. Activity in most of the heavy industries is still subnormal, and there is no limit, either in lack of capacity or lack of need for the goods they produce, to check their further expansion. There is a reserve of unskilled and semi-skilled labor still to be absorbed. Business credits are not expanded and no pressure for curtailment can develop on that account; on the contrary, money for business use is virtually the cheapest ever known, borrowers and lenders are both overcoming their timidity, and the great surplus of gold furnishes continuous evidence that the danger to business stability from the standpoint of credit is only that the forward movement may eventually run into an unwise credit expansion.

The Rise in Costs

Another comparison of interest is with conditions in 1923, preceding the brief slump which carried into 1924. By the middle of 1923 the recovery from the post-1920 depression had carried business above the "normal" line, wage advances had been made in many industries, and there was strong competition for labor in the building and other trades and numerous indications of higher prices. The rise in costs and prices impressed conservative opinion unfavorably, caused a slowing up of forward buying, and of new projects, and led to the recession which carried business temporarily below "normal" again in 1924.

Whether the present wage increases, the Social Security taxes, and the higher costs of raw materials, can be paid by consumers, or whether the higher prices will slow up the improvement, is a question which manufacturers are answering optimistically, but upon which the practical demonstration is still to come. Conservative opinion always views a rise of industrial costs with apprehension, because there is always uncertainty whether it can be passed on, whereas a reduction in costs, other things being equal, is a sure road to increased production and employment.

The price advances in cotton goods for the most part preceded the wage increases, and plainly have been no obstacle to a record volume of forward buying on the part of converters, wholesalers and distributors generally. However, the increases have hardly reached consumers, and manufacturers of house dresses and other garments ordinarily sold on a price appeal, and within a fixed range to which buy-

ers have become habituated, are represented as being uncertain as to the outcome. The wage increases in steel and woolen goods have directly caused price advances, and the acceptance of the new prices by consumers is still to be determined.

As against this uncertainty, the favorable elements have been given above. Compared with the first half of 1923, the chief difference in favor of the present situation is that business is not now above normal as a whole, but still somewhat below. The factors that were influential in bringing about the revival of industry in 1935 and this year manifestly have not expended themselves. If demand for cotton goods and products of the other industries which are abnormally active shows a natural decline, it is none the less certain that the deficit in houses, in railway and utility equipment, in machinery generally, and also in automobiles, house furnishings and similar goods, has not been made up.

The fact that work on new projects has been deferred during the past two years, and is still deferred, because confidence has been lacking, is the best assurance that there is much of this work yet to be done. Undoubtedly building would be more active if costs were lower, but due to the rise in rents and income building costs are less out of line than for several years past, and building was a mainstay of business improvement for many years after 1923, despite the general opinion that costs were too high. The fact that plant capacity of a few industries is now being fully utilized, including rayon, wood pulp, plastics and some other manufacturing lines, assures that new plant construction will go on even if buying slows down somewhat. In all industries the higher wage scales will increase the incentive for overhauling and installing new and efficient equipment.

The psychological elements in the situation are predominantly favorable. Business men have been under restraint for a long time, and for the present at least there is a notable rise in aggressiveness and courage. It is true that "business sentiment" is far from a reliable guide to the future. It has no power to prevent a corrective reaction after a period of over-buying; likewise it may change rapidly, under the influence of new developments, mistaken thinking, or of interferences from without the business system. Nevertheless, the state of business at a given time is in great degree what the state of confidence and enterprise make it. Both are now higher than in a long time, and both are infectious.

No one would claim that the handicaps are removed. There is no certainty that the foundation of business is sound as long as so much of the purchasing power is derived from the deficit expenditures of governments; there is evidence of deep-seated maladjustment in the persistent unemployment; and what unpredictable setbacks and new interferences may lie ahead is unknown. But business itself is demonstrating that forces powerful enough to go against the handicaps are in operation.

The Commodity Price Advance

The jump in staple commodity prices has come with somewhat unexpected suddenness. There was no lack of prediction of a rising trend of commodity prices, but little expectation of as sharp an advance occurring simultaneously in so many markets. Nearly all the important industrial raw materials have spurted, including the metals, textile fibers, rubber and hides, also some imported foods and a fair sprinkling of domestic farm products. Many have reached new high levels for the recovery.

The advances are due almost wholly to the strengthening of demand and forward buying, rather than to changes on the supply side of the markets. In most cases production is greater than a year ago, except where short crops have interfered, but the demand is eating into stocks on hand. Also, the rise is international in scope, with few exceptions. In fact, the international markets for wool, wheat and copper, all commodities receiving substantial tariff protection in this country, have taken the lead in forcing the American markets up. In the international commodity markets the demand from this country is of course very influential, but the improvement in consumption is world wide, due to the combination of better business and armament demands. The disposition to buy ahead is also increasing in other countries.

Of course, commodity markets, like a rise of business, can move too fast, and forward buying may be temporarily overdone even though the long trend is upward. It may not be amiss to repeat the general statement made in this Letter last month, namely, that there is room for a considerable increase in the production of most raw materials and farm products. In commodities whose production is uncontrolled the natural tendency of the higher prices will be to stimulate output. It is agreed by all observers that the Western farmers want no acreage restrictions for 1937, and that the grain acreages now contemplated will raise substantial surpluses over our own needs if growing conditions are favorable. According to preliminary estimates, the Winter wheat acreage seeded this Fall is an all-time high record. Cotton men concede the likelihood of a considerable increase in the cotton acreage next Spring, unless controls are invoked.

In the commodities whose production is controlled by agreements, it is risky to make assumptions as to the policies of the controlling authorities, but they have learned by experience the danger of forcing prices too high,

which would turn consumers to competing products and make enforcement of the controls among producers more difficult. The allowable production of rubber, copper and tin has been increased during the past month.

Money and Banking

The past month has seen a continued rise of the country's monetary gold stock and excess bank reserves. On November 25, the gold stock stood at $11,162,000,000 a new peak for all time, representing an increase of $376,000,000 since the Gold Bloc devaluation in September. Although part of this increase came from domestic production, the major portion was the result of gold imports, indicating that the United States is continuing to attract foreign funds, contrary to the rather widely held view that a re-alignment of currencies in Europe would reverse the capital flow and lead to some reduction of the volume of foreign money in this market.

As the new supplies of gold have become available, they have been bought by the Treasury, which has made payment by drawing on its balances in the Federal Reserve Banks. This has put Federal Reserve funds into the market and added to the volume of bank reserves. Inasmuch as the reserves required to be held against bank deposits did not increase in like proportion, the "excess" reserves rose further to $2,270,000,000 on the 18th, at which point they were approximately $460,000,000 higher than in the middle of August when a 50 per cent mark-up of reserve requirements was put into effect for the purpose of holding down a too rapid growth.

Possible Action on Excess Reserves

This continued rise of excess reserves over and above the level regarded last Summer by the authorities as healthful, taking account of potentialities for credit expansion, has been the occasion of renewed discussion as to the possibility of additional measures to keep excess funds within bounds. The Federal Reserve Board and the regional Reserve Banks are known to be giving consideration to the situation, and at the close of a series of meetings last month involving the Reserve Board, the Federal Advisory Council, the Presidents of the Reserve Banks, and the Open Market Committee, Chairman Eccles of the Reserve Board gave out the following statement:

> The board of governors of the Federal Reserve System met during the week with the Federal Advisory Council and later with the presidents of the Federal Reserve Banks. In addition, there was a meeting of the Federal Open Market Committee.
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> In the course of these meetings the business and credit situation was carefully reviewed. Particular attention was given to the fact that since the board's action last July* in raising reserve requirements there has been a continued and substantial increase of member bank reserves, resulting principally from a further large inflow of gold from abroad, so that member bank reserves are once more far in excess of legal requirements and of present or prospective needs of commerce, industry and agriculture.
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> Those charged with responsibility for credit and reserve policy are now giving careful consideration to the various problems raised by the effects of these reserves with a view to taking such action at such time as appears to be necessary in the public interest.

Supplementing this statement, Secretary Morgenthau announced that the December Treasury financing would cover $429,000,000 of Treasury notes maturing February 15, next, in order to "clear the decks" for whatever action the Reserve Board might wish to take with respect to excess reserves early next year.

The foregoing official statements give ample notice to the market that further action to control excess reserves must be considered a near-term possibility. That such action, if taken, is likely to be delayed until after the first of the year is suggested not only by the Secretary's statement, but also by the logic of the situation. The Treasury financing due on December 15 naturally would preclude action before that date. Moreover, in December, holiday currency requirements, together with tax collections and whatever new money the Treasury may ask for and receive in cash on the 15th, will in the normal course of events effect a substantial, though temporary, reduction in excess reserves. Not until after January 1, when much of this money will be coming back to the banks, are excess reserves likely to be a problem, hence the expectation that nothing will be done about them until at least that time.

Alternative Methods of Control

Whether, in the event of such a move, it would take the form of a reduction of the Government security holdings of the Federal Reserve Banks or another raising of member bank reserve requirements, the Reserve authorities have declined to say. At the present time the Reserve Banks hold $2,430,000,000 of Government securities, and could readily permit a portion of the shorter maturities to run off, probably without disturbance to the market and without seriously affecting Reserve Bank earnings, owing to the extremely low rate of return afforded by these issues. It is generally conceded that the power to change reserve requirements should be used sparingly, and the Reserve Board, at the time of the August increase, announced a policy of resorting to this method of control only infrequently —subject, however, to the following qualification: "Unless large additional increases in reserve occur through gold imports or otherwise, no occasion for further adjustments in reserve requirements are likely to arise in the near future". The fact is that large increases in reserve *have* occurred through gold imports.

* Announcement was in July; advance effective August 15.

Those who argue for an advance in reserve requirements do so on the ground that the heavy imports of gold since devaluation of the dollar have created a basic change in our monetary position that warrants unusual methods of adjustment. They point out that with excess reserves in January possibly equalling or even exceeding the Federal Reserve's portfolio of Governments, the situation is no longer amenable to control by open market operations alone. Under such conditions it is suggested that the advance of reserve requirements should be employed first when it will cause relatively little hardship, leaving in reserve the weapon of open market operations. This, being a familiar and accepted method of credit control, would be more likely to find acceptance in a period calling for restrictive action than would the more drastic step of changing the reserve regulations.

According to law, the Reserve Board has authority to raise reserve requirements by another 50 per cent of the amount required at the time the Banking Act of 1935 was passed, or by 33⅓ per cent on the basis of present reserve requirements. This would mean, on demand deposits, lifting the required percentages from 19½ to 26 per cent for member banks in the central reserve cities of New York and Chicago, from 15 to 20 per cent for banks in reserve cities, and from 10½ to 14 per cent for "country" banks. On member bank time deposits the increases would be from 4½ to 6 per cent throughout. Assuming for purpose of illustration that excess reserves in January reach a total in the vicinity of $2,400,000,000 to $2,500,000,000, and the Reserve Banks go the limit in raising reserve requirements, the cut in "excess" would be to around $800,000,000 to $1,000,000,000.

Undoubtedly, this would seem like a large reduction to a market accustomed to the huge totals of the past couple of years. It is pertinent to point out, however, that excess reserves of this magnitude would still be far in excess of levels prior to 1934, and amply sufficient to provide abundant and cheap credit for industry and trade, which must still be considered a major objective of Federal Reserve and Treasury policy. Following is a table comparing open market short-term money rates now and when last member bank excess reserves were $800,000,000.

Excess Reserves and Open Market Short-term Money Rates

	Av. Nov., 1936	Av. Jan., 1934
Member bank excess reserves	$2,220,000,000	$859,000,000
Call money	1%	1%
Time money, 60-90 days	1¼%	¾—1¼%
" " 4-6 months	1¼%	1—1½%
Commercial paper	¾%	1¼—1½%
Bankers' acceptances, 90-days, asked	3/16%	½%
Treasury bills	0.10%	0.67%

It may be well to bear in mind that the certainty of official action with respect to excess reserves has not been established. The authorities have not committed themselves, and undoubtedly will be guided by events.

A Method of "Sterilizing" Gold Imports

The attention given to the problem of excess reserves makes pertinent some reference to another method of "sterilizing" gold imports which has come in for some discussion. This proposal has to do with the method of payment by the Treasury for its gold purchases. At present, the Treasury pays for imported gold by drawing a check on its fiscal agent, the Federal Reserve Bank, subsequently replenishing its balances at the latter by the deposit of gold certificates issued against the gold as coverage. The effect of the completed operation, therefore, is to put into the market new funds obtained from an outside source, thus bringing about an increase in member bank reserves. In other words, gold imports tend automatically to increase the supply of money and credit unless purposely offset by Federal Reserve open market operations or an advance of member bank reserve requirements.

Under the procedure suggested, gold imports would be prevented from acting in this automatic manner. Instead of the Treasury paying for the gold by drawing on the proceeds of gold certificate deposits with the Reserve Banks, as at present, the Stabilization Fund would be authorized by Congress to borrow through the use of Government obligations. Thus gains and losses to the market on account of gold transactions would cancel out, leaving bank reserves unaffected.

It may be observed that the British Equalization Fund works in this general fashion. The Fund buys incoming gold and pays for it with funds raised by the sale of Treasury bills, thus preventing any expansion of deposits or reserves. Possibly the United States could obtain the same results were the Treasury merely to refrain from depositing gold certificates at the Reserve Banks against its gold purchases. In that event the Treasury would have to make good its Federal Reserve balances out of ordinary receipts and proceeds of borrowing, thus accomplishing the sterilization desired.

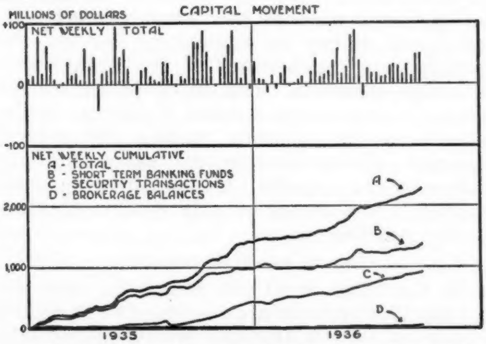
An objection to proposals of this nature is that they would entail an increase in the public debt and interest requirements. The cost, however, would be relatively small in view of the low level of interest rates, and perhaps might not be considered an excessive price to pay for avoidance of inflation. Another, and possibly more valid objection would be in the tendency to confuse still further the responsibility for credit control, already divided be-

tween the Treasury and the Federal Reserve Banks, not to mention the Federal Deposit Insurance Corporation and the Comptroller of the Currency's office. As a matter of principle, there is much to be said for a policy of concentrating this responsibility in the central bank.

The Problem of Foreign Funds

Fundamentally, it must be recognized that the problems created by gold movements, capital flights and excess reserves spring from the general state of fear and disorder existing in many parts of the world which has disturbed trade relations and diverted funds from their normal uses. This is in large part the explanation of the huge influx of alien funds into this market to which President Roosevelt has called public attention recently.

For some time the Treasury has been maintaining a record, based on weekly reports from banks, bankers, brokers and others, of the capital movement between the United States and other countries, the results of which, recently made public for 1935 and the first nine months of 1936, make a most interesting showing. According to these tabulations, there was a net inflow of foreign capital during the twenty-one months of $2,281,659,000, of which $1,353,072,000 net consisted of short-term banking funds, $905,429,000 of security transactions, and $23,158,000 of brokers' balances. This capital movement was distributed over the period as indicated in the accompanying diagram.



It will be noted that during the first nine months of 1935, the movement was principally one of short-term balances, but that beginning about October, 1935, there was also an accelerated flow into American securities. This was in conjunction with the outbreak of the Ethiopian war and the more definite development of the American bull market. During 1936 there was a continued movement of funds into American securities, but a leveling off in the inflow of bank balances until on towards midyear when the rise was resumed accompanying further war scares and developments in the Gold Bloc countries leading up to devaluation.

The classification of funds by countries is also of interest. As indicated by the following table, the largest net inflow was from or through the United Kingdom, with Switzerland next, followed by France and the Netherlands.

Net Capital Inflow, January, 1935 through September, 1936, by Countries

United Kingdom	$ 789,204,000
Switzerland	297,630,000
France	201,949,000
Netherlands	194,962,000
Germany	72,868,000
Italy	28,714,000
Other European	197,241,000
Canada	138,482,000
Latin America	159,926,000
Far East	195,015,000
Other	13,668,000
Total	$2,281,659,000

Taken together with the Department of Commerce report on foreign holdings of American securities at the end of 1935, the Treasury report indicates total foreign investments in this country at around $7,200,000,000, of which about $1,000,000,000 was in direct investments, $3,500,000,000 in marketable securities and $1,600,000,000 in short-term balances.

The heavy movement of capital indicated by these figures, while welcomed in the beginning as a sign of returning confidence in American securities, has become more lately a source of official concern, both on account of the present incentive to inflation and the danger of unfavorable repercussions on our markets and exchange rates in the event of sudden withdrawals at some future date. In the revised edition of his book, "The Reserve Banks and the Money Market," Dr. W. Randolph Burgess, Vice President of the Federal Reserve Bank of New York, draws an interesting parallel between the present situation with respect to gold and international balances and that of the twenties. We quote:

> The world is today suffering from practically the same disorder or economic and monetary instability as in the early twenties, and largely for that reason gold is again flowing to this country, and in amounts much larger than in the earlier period. The problem of those days has reappeared in magnified form. It is again twofold: how can the disorder that causes the gold flow be cured; and how can the gold be prevented from creating an over-expansion here?
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> * * * * *
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> The parallels with previous experience are extraordinary. When the Reserve System first began operations the member banks held $800,000,000 of excess reserves. Today they hold $2,500,000,000. The rapid gold imports of 1934 and 1935 may be compared with the imports of 1920 to 1924 except that the recent movement was about twice as large, $3,000,000,000 compared with $1,500,000,000, and took place in half the time and was added to an already large stock just increased by $2,800,000,000 through the devaluation of the dollar, and gold additions are being supplemented by substantial amounts of silver. The country's gold stock was $1,600,000,000 in 1914, $4,000,000,000 in 1929, and $10,000,000,000 in early 1930.

Suggestions to the effect that some curb be put on the movement of funds to this country do not appear to go to the heart of the trouble.

The movement is symptomatic of deep-seated disorder. Evidently, the real remedy lies in the removal of political uncertainties and re-establishment of economic stability in Europe and elsewhere throughout the world.

Banking Conditions and Markets

Member bank changes during the four weeks ended November 18 revealed a moderate counter-seasonal rise in "other" loans, indicating that business borrowing has extended beyond the usual seasonal period. Circulation figures, responding to gains in retail trade and payrolls, have been breaking all records save for the banking holiday. On November 25 total currency outstanding was approximately $600,000,000 greater than a year ago. Bank holdings of investments, including U. S. Government obligations, continued the decline generally in progress since last Summer.

Evidently the lightening of investment portfolios by banks had no dampening effect on the bond market, for prices of high grade issues moved forward following the election, presumably on the assumption of continued cheap money. Government bonds rose 1½ to 2 points, establishing new high prices all along the line. In addition to cheap money, the Government market has been affected favorably by the rapidly rising revenue receipts and improved budgetary outlook, while the prospect of an increased absorption of Government securities over the next few years by the Social Security Fund is not being overlooked.

A feature of the bond market during the month was the offering of $23,500,000 Argentine Government 4½ per cent conversion bonds at 92½. The favorable reception accorded this issue, the first step in a large refunding program, was regarded as recognition of that government's excellent credit record during the depression and as an indication of a more discriminating attitude on the part of investors with respect to foreign bonds. Funds obtained from the sale of this issue are to be applied to the payment on June 1, 1937 of the 6 per cent bonds due December 1, 1958. On November 27, the Argentine Finance Minister, Dr. Roberto M. Ortiz, announced as a second step in the conversion program the call of $36,778,500 of 6 per cent bonds due June 1, 1959 for payment June 1, next, the funds being provided from the Argentine Treasury. In accordance with the terms of the loan contracts money for redemption of both issues, together with interest, is now on deposit with the fiscal agents.

Our Declining Export Surplus

In a country which has had traditionally year after year and month after month a so-called favorable balance of trade, an excess of imports always makes news. Since the Spring of 1935 reports of that nature have become more frequent. In four months of 1935 the United States had a surplus of merchandise imports; this year the balance of merchandise trade has been the other way in seven of nine months.

Thus far in 1936 commodity imports have been $63,000,000 larger than exports, but there is still a possibility that we shall accumulate an export surplus in the last quarter. Ordinarily a sharp seasonal rise in exports takes place in the Fall. This year, however, the increase of 23 per cent in September exports over the August figures was more than offset by the gains in imports. Hence, for the full year 1936 our trade will undoubtedly be much more closely balanced than in 1935, when the export surplus was $204,000,000. This was the smallest surplus in forty years.

As late as 1928 we had an export balance exceeding one billion dollars, but with the onset of the depression and the contraction of foreign trade, the margin grew smaller, falling in 1933 to $214,000,000. A rise of 28 per cent in our exports the following year, 1934, created an export surplus of $464,000,000. This recovery may be attributed to the undervaluation of the dollar abroad and to the rise in prices of some of our raw material exports, particularly cotton. However, the stimulus provided by the undervaluation was only temporary. It gradually wore off as various foreign currencies were further devalued and as our prices began to rise. Moreover, the crop failure in 1934, plus the A.A.A. reduced our exportable agricultural surplus. In addition, the political changes in Europe have speeded the trend toward self-sufficiency, either on account of national defense policies or because of the unfavorable exchange situation. The fruits of these tendencies, Government control of foreign trade, barter exchange, bilateral trading, and general currency disorganization, increased the obstacles to our exports. Hence, the promising expansion was sustained only moderately during the last two years.

The Increase in Imports

On the other hand, our industrial recovery and the 1934 crop failure combined to stimulate imports of raw materials, semi-manufactures and foodstuffs, so much so that during the first nine months of this year the value of these classes of imports nearly doubled as compared with the same period in 1932. In volume, our requirements of many industrial raw materials have climbed back almost to 1929 levels. Imports of rubber, tin and wool are rapidly approaching pre-depression levels. We are more dependent on foreign paper base materials, imports of which have increased over 1929 in volume, but are getting along with less silk and hides.

Improved purchasing power has been reflected in heavier imports of foodstuffs of which we do not supply our own needs. Imports of coffee and cocoa were the largest and next to

the largest respectively on record during the first nine months of this year, while cane sugar now heads the import list, reflecting both the increased volume and higher prices. The drouth in 1934 also increased agricultural imports in 1935; but for the imports of wheat, barley, corn, cattle, meat products, butter, flaxseed and vegetable oils to supplement our domestic production, the value of our imports would have been about $120,000,000 smaller, and our excess of exports that much larger. This year's drouth will require additional imports of most of these products.

Still another factor has contributed to the recent narrowing of our export surplus. This is the rise in import prices, which since 1934 has been somewhat greater than in export prices. On the whole this rise in prices, affecting raw materials, is to be welcomed, even if it temporarily causes a reduction of the export surplus. It means a more normal relationship between the prices of raw materials and manufactured goods, and of course more purchasing power in the hands of the primary producers in this country as well as abroad, who in turn become better customers for our finished manufactures. As compared with 1929 we are still buying our imports very cheaply; we are paying about half as much for them in money, but getting only 13 per cent less in volume.

Shifts in Export Trade

Generally speaking, the world wide business revival has been the greatest influence upon our exports in the past three years; they reflect all the forces, natural and artificial, the inter-play of which has brought a number of countries to the threshold of prosperity.

As compared with 1933, exports to the British Dominions, which have more than doubled, have increased more than to any other part of the world. This is evidence that our trade stands to gain most where business improvement is most genuine. Politically and socially stable, the British Dominions as producers of raw materials have benefited from higher prices, and also from the industrial recovery of the mother country. After the British Dominions, the largest gains in exports had been to Latin America, due also to the improvement in prices of primary commodities.

Since business recovery has been larger on the whole in countries which are surplus producers of foodstuffs and raw materials, and also because of increased self-sufficiency of agriculture in Europe and decreased agricultural production in this country, our export trade has naturally shifted from crude to manufactured goods. This year almost 50 per cent of our exports consist of finished products compared with the average of 37 per cent for the post-war decade and less than 30 per cent for the years immediately before the war. Prior to the war about one-fourth of our exports consisted of foodstuffs; by 1929 it had declined to about 15 per cent; this year the percentage has dropped to 9 per cent. We have maintained our tobacco exports and have even expanded our fruit exports but our exports of meat and grain products brought us only $45,000,000 during the first nine months of this year, whereas in the same period of 1929, when prices were only about 25 per cent higher, we marketed abroad over $291,000,000 of these commodities. Raw cotton exports in the first nine months brought only $216,000,000 against $445,000,000 in the same period of 1929.

United States Imports
(In Millions of Dollars)

	Calendar Years			Jan.-Sept.	
	1929	1932	1935	1935	1936
Total imports	4,339	1,325	2,039	1,507	1,767
Crude materials	1,559	358	583	425	533
Crude foodstuffs	539	233	322	241	244
Mfd. foodstuffs	424	174	319	260	295
Semi-manufactures	885	217	409	292	360
Finished "	994	341	405	289	335
(1929 = 100)					
Volume	100	60	81	79	87
Value	100	30	47	46	54
Unit Price	100	49	57	57	60

United States Exports
(In Millions of Dollars)

	1929	1932	1935	1935	1936
Total Exports	5,157	1,576	2,242	1,537	1,704
Crude materials	1,142	514	683	405	418
Crude foodstuffs	270	89	59	40	43
Mfd. foodstuffs	484	152	157	106	108
Semi-manufactured	729	197	349	253	290
Finished "	2,532	624	994	732	846
(1929 = 100)					
Volume	100	52	58	54	60
Value	100	31	43	41	45
Unit Price	100	59	75	75	76

Undoubtedly we should have lost some of our agricultural exports in the past two years irrespective of our curtailment of production. Some of our best customers on the Continent of Europe have already become independent of foreign grains and fats. Their remaining agricultural imports have been purchased from those countries which take in exchange their manufactured products. Thus in 1935 we supplied less than 5 per cent of the German lard requirements, against almost 90 per cent in 1929. As late as 1930 Germany bought from us about 1,300,000 bales of cotton, or three-fourths of her requirements. In 1935 we shipped to Germany only 345,000 bales or less than one-fourth of her needs. Brazil, Argentina, Turkey and Peru and a long list of smaller countries increased their exports of cotton to Germany several times, not because their cotton was better or materially cheaper, but because they were willing to accept in payment manufactured goods on barter terms. Actually Germany paid more for this cotton in goods than she would have paid for our cotton in cash.

This is an example of the distortion of normal trade relations brought about by the depression and by the desire for self-sufficiency as a means of war preparedness. Tariffs, quotas, barter, special import licenses and other devices, adopted for the purpose of securing advantages over other countries, have ended in reducing the trade of all. Certain exceptions, however, must be noted in this general trend toward nationalism. The reciprocal trade agreements program of the United States, inaugurated by Secretary Hull, has represented a major effort directed at the breaking down of international trade barriers. Already treaties have been concluded with fourteen countries, including France and Holland and their colonial empires. Also, with the diminishing severity of the depression, progress has been possible in other directions. The new currency stabilization agreement concluded by the Governments of the United States, Great Britain and France, and lately joined by the Governments of Belgium, Switzerland and Holland, represents probably the most important step so far taken towards freeing international commerce. The conference of American republics in Buenos Aires this month will, it is hoped, accomplish further important results in improving international relations, both politically and economically.

Effects on Balance of Payments

Since our merchandise trade is a very large item in the current payments due to and from this country, the reduction in the export surplus necessarily affects the balance of these payments very considerably. Moreover, there are other influences tending to reduce the net balances accruing to this country on current transactions (irrespective of capital movements). Industrial recovery has been reflected not only in a greater demand for foreign commodities, but also in a greater expenditure for foreign services. The bill for shipping services performed for us has been growing larger. There has been more travel abroad. This year the number of overseas tourists approached the best pre-depression years; and devaluation in the Gold Bloc countries will further stimulate travel. Only immigrant and charity remittances have declined persistently, despite improved business. Exchange restrictions abroad and the gradual dying out of the older immigrant generation may be offered as the most plausible explanation for this tendency. However, with business improving, payments for commodity imports as well as for services are likely to increase further.

Next to our merchandise exports, the largest single item which provides us with means of making payments abroad is the interest and dividends received from our overseas investments. In 1929 nearly one billion dollars was received by us from this source. In 1935 these payments shrunk to $521,000,000 due to lower earnings as well as to defaults and reductions in our foreign investments. On the other hand our payments to foreigners on their investments in this country have shown a considerable growth lately as a result of increased purchases of American shares since the Spring of 1934 and a tendency for dividend rates to rise. Thus our net balance on interest and dividend account shows a narrowing tendency.

Deficit on Commodity and Service Transactions

Our considerable purchases of silver since the Midsummer of 1934 should rightly be included with our commodity trade, as formerly, rather than being treated as a treasure movement, as they are at present. Silver could hardly be used in the settlement of our international obligations, but would have to be sold at the market price prevailing at the time of need. Silver purchases have been sufficient to turn our balance of payments on commodity and service accounts in 1935 into a deficit of

U. S. Trade and Service Accounts Including Silver Purchases, 1924-1935
(In Millions of Dollars)

	Net Receipts				Net Outpayments					
Date	Mdse. Trade	Interest and Dividends	All Other	Total	Tourist Expend.	Immigrant Remittances	Shipping Services	Silver Purchases*	Total	Net Balance
1924	+ 981	+305	+273	+1,559	—500	—355	+ 8		—847	+712
1925	+ 683	+355	+276	+1,314	—560	—360	— 8		—928	+386
1926	+ 378	+467	+134	+ 979	—498	—264	—61		—823	+156
1927	+ 681	+519	+156	+1,356	—528	—255	—66		—849	+507
1928	+1,037	+534	+ 62	+1,633	—552	—276	—80		—908	+725
1929	+ 841	+565	+ 10	+1,416	—638	—265	—66		—969	+447
1930	+ 782	+616	+144	+1,542	—602	—215	—96		—913	+629
1931	+ 334	+536	+ 20	+ 890	—456	—202	—72		—730	+160
1932	+ 289	+393	+ 32	+ 714	—375	—163	—45		—583	+131
1933	+ 225	+384	— 25	+ 584	—221	—132	—16		—369	+215
1934	+ 478	+367	+ 27	+ 872	—245	—131	—35	— 86	—497	+375
1935	+ 236	+375	+ 40	+ 651	—292	—115	—36	—336	—779	—128
6 mo. 1936	— 9	+190	+ 17	+ 198	—115	— 57	—18	—116	—306	—108
9 mo. 1936	— 63	......	......	....	......	......	....	—147	......	......

* Note: Up to 1934 silver transactions were included in merchandise trade.
Sources: Trade Information Bulletin No. 833, "The Balance of International Payments of the United States in 1935". Also release of the Finance Division of the Bureau of Foreign & Domestic Commerce, dated Oct 4, 1936.

$128,000,000. On the basis of official estimates it appears that during the first six months of 1936 trade and service accounts ended with a deficit of $108,000,000, again incurred chiefly by silver buying. During the first nine months we spent abroad for silver almost $150,000,000, of which more than half was in the first quarter. As will be seen from the table given, the balance in our favor resulting from commodity and service transactions declined quickly after 1930.

It should be borne in mind, of course, that capital imports during this period have covered the deficit on current transactions many times over, as evidenced by net gold imports since January, 1934, of almost four billion dollars. The deficit in commodity and service payments is of minor significance as long as it is covered by these capital imports, but if capital movements should recede to normal proportions the trade figures would dominate our international balance sheet, and the present situation differs from any this country has ever known.

The Outlook

While it is improbable that we shall know in coming years the large trade balances and the favorable margin on current transactions that were the rule in the past, and the outlook for the next twelve months is for a deficit, it does not follow that a minus sign will permanently appear on our international balance sheet. A good many factors which have tended to reduce the surplus are temporary and will eventually correct themselves. A single good crop year, perhaps in 1937, will greatly alter the trade balance, making us again independent of certain foreign foodstuffs and leaving a surplus for exports. Further improvement in the position of the countries producing raw materials, particularly in Latin America, is bound to be reflected sooner or later in a rising income from our investments.

The movement of our internal prices in relation to prices abroad is likely to be of more eventual importance than the trade shifts which have thus far occurred. A further general devaluation of international currencies or a sharp rise in our internal prices due to inflationary influences would have a much more disturbing and lasting effect on our international accounts.

Even if the balance against us should continue, the inability to purchase gold or to have a surplus for reinvestment abroad out of non-capital transactions should not cause apprehension. With over fifty per cent of the world monetary gold in our vaults, continued gold imports are a menace rather than a benefit. There is now too little gold left outside of this country, Great Britain and the former gold bloc countries, for the central banks of some 47 countries, excluding the foregoing, hold less than 20 per cent of the world's gold.

As to a surplus for reinvestment abroad, the outlet for our capital is limited to a very few countries under existing legislation. A loan to Argentina or Australia, two countries which are most likely to resume foreign borrowing, would hardly entail a transfer of gold, but would be spent for equipment.

It would be of benefit to us as well as to the whole world, if for a few years we were to spend our international earnings for commodities and services rather than for purchases of gold. Without making ourselves poorer, we should resume the true role of a creditor nation which we have refused thus far to follow.

The Economic Problem

The great vote for President Roosevelt's reelection must be accepted as an expression of confidence and a bar to merely factious or partisan opposition to his leadership. Doubtless the business recovery of the last two years has been an important factor. The people now are eager to turn from political strife to the extension and maintenance of prosperity.

The President entered upon his office in a time of great economic disorder and depression, worldwide in extent, when all governments were resorting to extraordinary measures to mitigate the distress of their peoples. Now that natural recuperative forces are clearly in action, it may be assumed that the emergency measures will be of diminishing importance and that the President, with the large party majority behind him, will desire to "consolidate" both the political and economic gains.

How and why do these emergencies occur? When the depression spread like a contagion from industry to industry and country to country a cry went up that the "economic system" had "broken down," and must be radically made over, but this had been said in every previous depression, all of which were succeeded by periods of prosperity, rising to levels of common welfare unknown before; and now the greatest of all depressions is passing.

The Principles of the System

That the system is open to the charge of instability must be admitted, but the fact that, like the political system, it is a voluntary association of individuals who are free to change their minds, and also a progressive system, involves a degree of instability. The long struggle for social progress has been characterized by insistent demands for freedom of individual initiative and action, and it is not clear how far we want to reverse ourselves on this. On the other hand, the modern economic system is dependent upon order and cooperation among its members.

There could be no advance in learning or industry without the specialization of labor and the exchange of knowledge and services.

The interdependence of all parts of the economic system is as certain as any of the natural laws upon which our existence depends.

The historic record is a continuous story of social advancement: new arts, new services, new products, new employments, new enjoyments, and always new possibilities giving zest to life. Within the range of memory electricity, the telephone, the automobile, the moving picture, the radio, the aeroplane have been developed into common use, and every industry rendering services to the public continuously made over by improvements. Steel and its alloys, the oil industry, modern printing, modern paper-making, the modern newspaper, modern engineering, modern plumbing, modern heating and refrigeration, and so on without end, are of the same period. Moreover, life has been lengthened, health protected, hygiene, medicine and surgery advanced, education extended, culture broadened, and the common standard of comfort and usefulness has been raised. And all of this has resulted from freedom of individual initiative, with specialization in research, learning and industry—vital principles of social progress.

The Complexity of the System

The complexity of the system, due to growth in the volume and variety of its services, is an evident cause of misunderstandings and disagreements. In the days of production by hand tools and of trade between neighbors, the economic system was all open to view, but when the materials of industry come from all parts of the world, when thousands of workers are employed by thousands of shareholders without any personal relations, and when industries, products, and services are constantly changing—and prices, wages and profits with them — the possibilities of misunderstanding and disagreements are infinitely increased. Nevertheless, we cannot abandon the system, for its complexities result from its benefits.

The growing importance of capital in production doubtless is a major cause of misunderstandings but the use of capital is in increasing the productivity of labor and also lessening its hardships. All capital investments originate in the employment of labor, as seen in the construction and equipment of railroads, factories and useful works of all kinds; moreover, these works afford lasting employment to labor in the production of goods and services for general use; and, finally, the wage-workers themselves are the principal purchasers of the products and not only want them but would like to have more of them.

Thus, the gains of technical progress go ultimately to the great body of the people; proof of this is afforded by the leading industries mentioned above, and particularly those in which large capital is required.

The Iron and Steel Industry

The iron and steel industry is often mentioned as one that in its nature is monopolistic, and notable fortunes made in it are named as conclusive proof; but the last month an event has occurred which has bearing on this, to-wit, the opening of the great bridge across San Francisco-Oakland Bay. Great bridges are triumphs of engineering science, and have marked the progress of all the physical sciences. This one is not only the greatest bridge in the world physically, but in the versatility of its engineering, including all features of construction. And it is a surpassing monument to the iron and steel industry.

The first bridge on this continent to win world fame was the Victoria Bridge over the St. Lawrence River near Montreal, completed in 1859. For many years pictures of this bridge appeared in American school books as one of the most notable engineering structures in the world. It was built of wrought iron, tubular in design, 16 feet wide, carried a single railroad track and was designed for a train load of 1 ton to the linear foot. The iron work of the original bridge (from England) weighed 9,044 tons, and the total contract price was $6,813,333. In 1898 this superstructure was torn down, foundations enlarged and a steel superstructure erected, and named the Victoria Jubilee Bridge, which stands today. This is 6,592 feet long, about 69 feet wide, carries two railway tracks, an electric car line, and a vehicular highway 16 feet wide, and was designed for a train load on each track, of two locomotives weighing 284,000 lbs. each followed by a train load weighing 4,000 pounds per foot. This bridge required 44,000,000 pounds of steel (22,000 tons) which came from the United States, and the total contract price for the reconstruction was $1,883,678.

The difference in structure and cost of these two bridges measured approximately the development of the steel industry in Andrew Carnegie's time, although the wages of labor in both steel-making and bridge-building were much higher on the second bridge than on the first. The principal reduction in cost was in the price of steel, and mainly due to the Bessemer process, but doubtless improvements in construction methods also were a factor. Declining prices of steel enormously increased its use for all purposes, and Carnegie in meeting this demand built up the vast Carnegie works out of the profits. They were built over and over continuously in his time, to conform to the advance of the industry, and at the time of their sale represented one of the greatest private fortunes ever accumulated; but it is safe to say that they would be worth practically nothing today, if the policy of constant rebuilding out of the earnings had not been

continued to the present time. As a result of a recent revaluation of assets, $270,000,000 was charged out of the consolidated accounts of the United States Steel Corporation last year. Replacement costs are part of the cost of the products but prices are steadily reduced.

Now comes the San Francisco-Oakland Bay bridge, bringing the industry down to date. In only the details given above can comparisons be made with the Victoria bridge and its successor, but the San Francisco Bay bridge has two decks, one above the other, each 66 feet wide. The top deck has six lanes for automobiles and the lower deck has 31 feet of roadway for three lanes of trucks and buses, also two electric railway tracks, with both third rail and trolley wires. This bridge has a "live road load" capacity of 7,000 pounds (3½ tons) per linear foot, and provides for 40-ton trucks and 70-ton interurban cars.

Beyond this, comparisons do not go, but this bridge is 8¼ miles long, of which 4½ miles are over water, and in type of design includes suspension, cantilever, through truss, deck truss, concrete viaduct and subways. It has 51 piers, the deepest of which goes down 242 feet from the water's surface to bed rock, while the suspension towers rise 470 or 515 feet above the water. It contains 200,000 tons of steel, and is stronger for its weight than the earlier bridges, on account of new steel alloys; it has 1,000,000 cubic yards of cement and has cost $77,600,000, including approaches, which compares with $60,000,000 for the George Washington Bridge, New York City. It was built by subsidiaries of the United States Steel Corporation for the California Toll Bridge Authority representing the State of California and financed by a sale of bonds to the Reconstruction Finance Corporation. Tolls approximating those now charged by ferries will be charged until the debt is paid off, after which the law says it shall be free to the public, with maintenance charges met by gasoline tax revenues, as in the case of other highways. It is estimated that the bridge will be free of debt in twenty years.

This bridge and another over the Golden Gate, now under construction, Boulder Dam with its 271 miles of power line, the recent bridges and tunnels about New York and similar works elsewhere, illustrate benefits that will belong to millions of people in perpetuity, made possible by developments in the economic system within very recent years. They are fruits of individual initiative and specialization in research and labor.

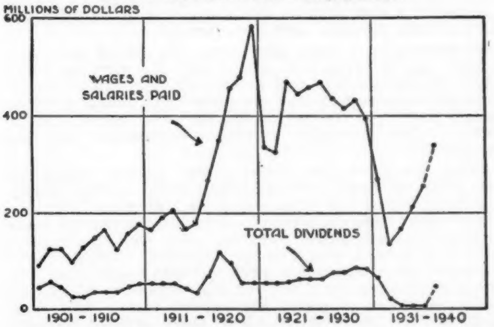
The Division of Benefits

The aggregate number of employes and investors in the steel industry are about the same, (approximately 500,000 of each) but the beneficiaries of the steel industry include the entire population, for steel is used in practically all production. Everything that enters the home has been cheapened by the improvements in making steel, not once only but in many ways, for it enters into every machine, into all modes of transportation, into every house and its furnishings and into all the costs of living.

The heavy capital requirements for producing steel are thoughtlessly made the basis of an assumption that the industry is a "monopoly," but justifiable use of that term applies only to an exclusive position, giving power to impose an unjustifiable price. The profits of the steel-manufacturing corporations are known, for like all corporations they must report their business in detail to the United States Government. The net earnings of all iron and steel companies for the five years 1926-1930, as shown by Treasury reports, averaged 4.84 per cent of gross income. A similar calculation for the largest twenty steel companies for the same years, taken from their published reports, shows an average net to gross of 8.76 per cent. These were better than average business years, particularly for the steel companies of large capacity. The average net earnings of all corporations in the United States doing business for profit, in those years, were 5.96 per cent of gross receipts. The steel industry is less stable in earnings than many lines of business, on account of its dependence upon construction. In the four years 1931-1934 the industry had no profits, but ran heavily behind.

Mr. E. G. Grace, President of Bethlehem Steel, recently emphasized the rapid changes in steel products and methods, in response to the

United States Steel Corporation



Note: This chart shows by one line the movement of aggregate wage and salary payments of the United States Steel Corporation from its organization in 1900 to 1936 (estimated), and by another line the aggregate of dividend disbursements. Peak of the former was in 1920, at crest of the War boom; peak for dividends was in 1917, a war year. Dividends have been paid only on preferred stock since 1932 and with the annual rate reduced from $7.00 to $2.00 in 1933, 1934 and 1935, but returned to $7.00 in 1936; the rate on common was reduced from $7.00 to 50 cents in 1932 and nothing has been paid since. The corporation had deficits of $71,175,704, $36,501,123 and $21,667,780 in 1932, 1933, and 1934 respectively, all dividends being paid from previous earnings.

needs of the industries. He mentioned the special equipment required for automobile sheets as costing the steel industry $200,000,000. Such special equipment is provided to reduce the cost of steel and the savings are passed on to the consuming manufacturers and eventually to the consuming public in lower prices. Mr. Grace said that the average price of steel products in 1936 had been $11 per ton lower than in 1923, which means a saving to the public of approximately 20 per cent, or $300,000,000 per year, and not only are those savings perpetual, but such improvements become the basis of more. What do the profits amount to, in comparison with these savings to the public?

Steel-Making a Science

The fact that steel-making has become a science, directed by experts in chemistry, is scarcely appreciated by the public. The composition of every steel specification is varied to suit the use. Mr. J. H. Van Deventer, editor of the "Iron Age," himself a graduate of the industry, in an address before the National Metal Trades Association, on April 22, 1936, said many interesting things about it, of which we can quote only as follows:

> When I was starting my shop career some 33 years ago, we had two kinds of steel; hard and soft. The soft steel was used to make things of, the hard steel to make them with. * * * The steel maker has graduated from the family doctor class, who fed all patients from the same bottle of pills, to the specialist who writes a prescription or fills one. One producer of steel has over 1,500 different alloys listed on cards and made-to-order for various customers. * * * Consider, for example, the impetus given to alloy and metallurgical development by our one metal trades product, the automobile. Early models were merely rebuilt carriages and were made up of materials then available, i.e., wood, cast iron, wrought iron, etc. * * * Exemplifying the shift to alloy construction, the car of 1911 used about 11 different alloy steels whereas the car of today will be made up of over 80 different alloys, both ferrous and non-ferrous.
>
> Various alloys have also been developed for particular use in airplanes. Originally the airplane used what the automobile had developed, but subsequently went its own way to produce particular constructional metals suited to its particular purpose, namely, light weight, high strength, corrosion resistance and dependability.
>
> Thus we have two great metal trades industries that have produced innumerable alloys. It was chiefly the demands of the automobile and airplane that inspired this research, which in turn revolutionized steel making and all metal working, and even made possible the recent changes in railroad rolling stock. Automobiles in the lower-price classes would cost five times what they do if not for the development of one series of steels, namely, high-speed tools. And they could not be produced at all in their present designs were only the original carbon steels to be had. We have thus a great industry growing, more men working, and more wealth being distributed because industry has turned to small problems and worked and produced metals to fill the demands made by these small problems.

All of the important industries have histories similar to that of steel. The locomotive and automobile were begun as crude power plants on wheels, the first as an upright engine pulling a stage coach, and the auto as a horseless carriage or buggy. Many minds worked on them, many companies were formed, millions of dollars were hopelessly sunk, and many names well known in earlier years have disappeared. Gradually the field of contestants has lessened, until "monopoly" talk is heard, although there remain plenty of models to choose from and prices continue to fall, while wages tend upward. More and more capital is required to accomplish further price reductions while putting more value into the product. Mr. Cameron, radio spokesman for the Ford Company, said of 1935 that the average capital investment required per employe, in order to keep that organization going, was $9,007.37, and that the aggregate of sales averaged $6,979.49 per employe. Furthermore, he itemized the distribution of this income as follows:

> Fully 94 per cent of it has gone for wages and materials; and after taxes and depreciation were paid, one and a half per cent remained for the Company. That is, out of every dollar of income from sales in the year ending September 30, our own and other employes received 94 cents; the Ford Motor Company received 1½ cents.

Had he gone on with a breakdown of the Ford Company's 1½ cent share it would have been shown that in the past the greater part of this has been used to enlarge the plant and give more employment.

This is the record of one of the most successful industrial companies. The reader may surmise the probable profit rates of others in its line. Why are they so small, when competitors are so few as to suggest that they have a monopoly? Is not the answer partly in an inborn urge to excel, and partly in the fact that if any competitor loses favor with the public it will go the way of so many predecessors? The industry is dominated by conditions to which individual members must conform, as truly as are the members of its assembly lines. The outstanding fact in this industry, as in iron and steel, is the extraordinary services to the public—not the fact that great fortunes have been made. If the industries had been owned by the public through the government, no less capital would have been required, and no better plan of obtaining it could be found than by retaining it from the savings the industries were accomplishing for the public.

Unemployment and Low Incomes

Why, then, the unemployment and poverty problems, admitted to exist? The first reply is that unemployment and poverty were known long before the modern economic system could be charged with them, and that notwithstanding the vast increase of population made possible by the "machine civilization" they have been greatly mitigated by it. Formerly the principal relief for the masses was by the high death rate, but in modern times vast numbers are supported by new industries and employments in a state of security and comfort before un-

known. Moreover, the rise in the common standard of living has stimulated hopes and expectations, and made all classes more sensitive to suffering and anxious to relieve it.

But the gains made possible by the modern economic system cannot be had without compliance with the principles upon which the system itself depends. This is as true of the system as a whole as of any single industry or any of the system's structures or machines. In every kind of an organization the parts must work together harmoniously or the productive capacity will be partially "unemployed." Nothing happens without a cause, and nothing but an abnormal and prodigious upheaval of the world-order could have caused the overwhelming disaster to industry and trade that has resulted from the World War. The War, with its far-reaching disturbance of economic relations, was the only adequate cause. Last month an account was given of the agreement between the Governments of the United States, France and Great Britain for the stabilization of their currencies. The most significant sentence in the French proposal was that stating the purpose to be "a reestablishment of a lasting equilibrium between the various economic systems." All nations were invited to cooperate with the tripartite movement, and all have given assurances which signify general agreement that the disorder in the currencies was caused by the disruption of trade relations resulting from the War. General recognition has been given that the most disturbing effects were caused by the worldwide disruption of price relations between agriculture and the more highly organized industries. The latter, more successfully than the former, were able to maintain nominal wages and prices, but they could not maintain employment, because the purchasing power of the mass of consumers had fallen. Now farm purchasing power has been restored, and Secretary Wallace frankly says that short crops and the clearing away of troublesome surpluses have been an important factor, by restoring reciprocal trade. The essence of his comment is that the depression "has demonstrated the importance of industrial prosperity to the farmer and of farm prosperity to the industrialist."

This is the same principle set forth in the French proposal, and President Roosevelt has emphasized it again in his recent letter to the Secretary of Commerce, by saying: "We will, I hope, pass into the next period of our Administration by looking to a wise and more equitable balancing of these inter-related segments composing our economic and social life." The President thus has sounded the note of economic harmony, stability and prosperity, and should have the cooperation of every element in the economic system. But this will depend mainly upon the "segments" themselves.

The Danger from Rising Costs and Prices

Cooperation depends upon mutual confidence and an understanding of mutual interests. Secretary Wallace has expressed apprehension that the present state of reciprocity between the farmers and other groups may not be lasting. A disruption of present relations may be caused either by a fall of farm products or a rise of products and services that farmers must buy, and both of these changes are possible. If the recovery of normal purchasing power by agriculture has been a prime factor in the general restoration of employment in the other industries, there is danger that a general fall of farm purchasing power may cause unemployment, as before. As Secretary Wallace says, present prices of farm products are drouth prices, and to make them the basis of a general rise of prices will be building on an insecure foundation.

Announcement has been made that at the opening of the new Congress a bill to establish the six-hour day in all railroad services will be introduced, and pressed for passage. The avowed purpose is to afford employment to former railroad employes now unemployed, but the effects must be to largely increase the cost of railroad service, which in its far-reaching effects would surely tend to increase the aggregate of unemployment.

Which class in the aggregate—employers or employes—gains most by industrial progress an increasing production of necessities and comforts, the lowering of living costs, etc., and which loses most by all derangements and disorders which slow down or obstruct the services of the economic system? Which class constitutes the largest body of consumers?

Nothing is more certain than that all the groups of the economic system are supplying each other, and that prosperity depends upon the orderly and truly reciprocal exchange of services. Moreover, it is a fundamental mistake to believe, as so many do, that the most important relationship is that between employers and employes in the different industries; in fact the most important relationship is that *between the groups* (employers and employes of each group together). The relations between employers and employes of single industries are comparatively simple, and usually adjusted without widespread disturbance; unemployment on a large scale generally results from causes outside of this relationship—as illustrated by War. Always it is because the "system" is disorganized and "team-work" is lacking.

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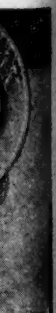

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